

**U.S. Department of Commerce
National Oceanic and Atmospheric Administration**

**ACCOUNTING FOR REAL PROPERTY
POLICIES AND INTERNAL CONTROL PROCEDURES**

US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
(Last Revised: 7/23/02)
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Documentation Hierarchy for Real Property Files**

Some real property files contain different source documents that provide conflicting information concerning real property acquisition values and dates. To rectify this problem, NOAA has established a hierarchy outlining the order of precedence by which sources of supporting documentation would be accepted as accurate.

Real Property obtained prior to Fiscal Year 1994

For all properties acquired during FY 1993 and prior, the files should contain the Supporting Documentation Rationale Sheet (See Attachment 1) with the appropriate supporting documentation.

- 1) If additional information exists in the files which contradicts the supporting documentation behind the rationale sheet, a memo should be included stating which document is most reliable and why.
- 2) Some files contain several documents supporting the acquisition date, acquisition cost, and ownership; and agreement is not always evident. The files should contain a memo clarifying which documents are the basis for the date of the acquisition and the acquisition cost and why they are the most reliable.

Unsupported Values

Leases or assets with unsupported values will be tracked with a hard copy file and noted in RSMIS with a tickler comment. This file should agree to the amount in the property file. The property and the amount will be reported to headquarters. Headquarters will assemble the data and forward the information to the Finance Office to be reported in the footnote disclosure.

Owned Real Property obtained subsequent to Fiscal Year 1993

The files for real property acquired subsequent to Fiscal Year 1993 should contain the deed for land. For buildings and structures, the file must contain the beneficial occupancy date and the final invoices or other documentation of acceptance.

Files containing Other Agreements

If the file contains other types of agreements (i.e. mineral rights, oil/gas rights, grazing rights, NOAA is the lessor, etc.), supporting information must be included in the file to properly document these other agreements.

Declaration of Taking

If the land was acquired via “Declaration of Taking,” then the acquisition date is the date that the court signed the settlement document. Also, the acquisition cost includes all costs paid per the settlement document or the declaration, plus any additional costs to acquire the land including preparation costs.

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Classifying Property as Real or Personal**

Background

The chief determination in classifying property as real or personal is whether or not they constitute a temporary or permanent improvement to the land. 41 CFR Sect. 101-47.103-12(5)(b) (Disposal of real property) excludes “prefabricated movable structures” from the definition of real property when slated for disposal. Trailers, garages, modular buildings, and generators meet the definition of a prefabricated structure or item and should be classified as personal property.

NEXRAD Towers and Upper Air Inflation Buildings

NEXRAD towers should be classified as personal property. Upper Air Inflation Buildings are to be recorded as personal property if NOAA owns the asset. If it is not possible to determine the cost of an Upper Air Inflation Building, the estimate developed by the CASC engineering office will be used. The file should contain the memo documenting the estimate and the reason actual costs could not be provided.

If an Upper Air Inflation Building is part of a lease with a Weather Forecast Office (WFO) it will be recorded by real property as part of an operating or capital lease. KPMG has agreed with this treatment based on discussions held at the Real Property Training Conference in Seattle, Washington during June 2-4, 1998. This policy will require disclosure in the lease footnote.

Trailers, Garages, and Modular Buildings

As noted above, trailers, garages, and modular buildings, and similar prefabricated structures are to be classified as personal property.

Generators, Wiring, and Cabling

Generators are to be considered personal property; they are by definition auxiliary, supplemental, temporary power sources for a facility. They are mounted on their own pads, in their own housing, and usually have minimal connection points to the building’s systems.

Wiring and cabling improvements, such as upgrades to electrical, telephone, or computer systems, typically do not extend the useful life of a real property asset. Unless installed during the initial construction of a building, in which case they should be included in the acquisition cost, these improvements will be expensed. These improvements are usually abandoned when no longer needed.

Security Equipment

Security equipment, which includes cameras, closed circuit televisions, magnetic card readers, computer equipment, and building access control systems, is considered personal property.

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Useful Lives**

Purchases of \$200,000 or more, with an estimated useful life of 2 or more years are capitalized. As the useful lives of these assets decline through either physical wear and tear from operations, and/or deterioration, they are depreciated. SFFAS #6 defines useful life as the “normal operating life in terms of utility to the owner.” Moreover, it is the period that the property is expected to be economically useable by the entity.

The useful life of an asset can be based upon the “IRS, Recovery Period for Common Assets” and the guidelines from OMB Circular A-76 Supplement, Appendix C that is used for capital improvements.

- Buildings and Structures
 - Temporary Buildings and Structures 10 Years
 - Wood Building and Structures 20 Years
 - Metal and Prefab Buildings/Structures 30 Years
 - Masonry Buildings and Structures 40 Years
- Construction Materials 40 Years
- Electrical Power and Distribution Systems 15 Years
- Plumbing Fixtures and Accessories 15 Years
- Heating, Air Conditioning and Ventilation 10 Years
- Industrial Boilers 10 Years
- Dryers, Dehydrators, and Anhydrators 10 Years
- Architecture and Related Metal Products 10 Years

If the asset has special considerations or is not listed, a memorandum from an engineer should be in the file documenting the useful life.

Leasehold Improvements

Improvements to leased property should be capitalized if the improvements meet the capitalization criteria. NOAA should depreciate these costs over the remaining life of the lease or the useful life of the leasehold improvement; whichever is shorter.

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Internal Control Policy
Interim RSMIS Solutions**

Recording Leases That Do Not Begin on the First of the Month

RSMIS cannot prorate lease dates if the beginning lease date is not on the first day of the month. RSMIS will calculate the lease term on a month-to-month basis rather than on a daily basis, and the calculations will round to the beginning or end of the month in determining payments for leases that begin on dates other than the first day of the month. Therefore, if a lease inception date falls between the 2nd and the 14th of the month, RSMIS will round back to the first day of that month. If the date falls between the 15th and the 31st of the month, the RSMIS calculation will round the inception date to the 1st of the following month.

Indefinite Leases

All leases in RSMIS having indefinite expiration dates will be flagged with an expiration year of 9999 so that RSMIS will show current year cost and the projection for the next fiscal year. Leases and all other agreements over \$200,000 in holdover will be given a defined period for expiration or, if no period can be determined; they should have their expiration dates extended to the end of the current fiscal year.

Stewardship PP&E

RSMIS does not have indicators for identifying heritage, federal mission, and stewardship assets, which must be reported under FASAB Standard #6. Per discussions held with NOAA Finance during the Real Property Conference in Seattle, WA on May 18-20, 1999, this information will be collected via data calls to NOAA ASC's. **However, the Real Property office will only report stewardship PP&E if the property contains a Real Property interest.**

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Capitalization Threshold**

NOAA capitalizes all real property items with acquisition costs of \$200,000 or greater. However, this does not apply to land assets, as land does not depreciate, so land will **always** be recognized as a capital asset and reported on the balance sheet. This amount was set in June 1998. Prior to June 1998, the capitalization threshold was \$25,000. The RSMIS property module shows the acquisition date and cost of all real property items owned by NOAA regardless of the acquisition cost.

Effective with the FY02 Year End Close, the RSMIS depreciation module must contain all NOAA owned land assets regardless of acquisition cost along with all other real property items whose acquisition cost is \$200,000 or greater. With the exception of land (which does not depreciate), the depreciable basis for all real property items equal to or greater than \$200,000 will be the original acquisition cost of the item and the original acquisition date, except when the assets are acquired from a prior federal entity as described in the Transfer of Real Property to NOAA from another Federal Entity section of this policy.

Assets are to be depreciated over their useful lives by the straight-line method. Accepted useful lives are contained in the Useful Lives section of this policy.

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Deferred Maintenance**

Definition

“Deferred Maintenance” is maintenance that was not performed when it should have been or was scheduled to be and which, therefore, is put off or delayed for a future period.

“Maintenance” is described as the act of keeping fixed assets in acceptable condition. It includes preventive maintenance, normal repairs, replacement of parts and structural components, and other activities needed to preserve the asset so that it continues to provide acceptable services and achieves its expected life. Maintenance excludes activities aimed at expanding the capacity of an asset or otherwise upgrading it to serve needs different from, or significantly greater than, those originally intended.

Measurement

Amounts reported for deferred maintenance will be determined using the “Condition Assessment Survey” method. A condition survey is a periodic inspection of real property to determine its current condition and to estimate costs to correct any deficiencies.

Condition Assessment Survey

A Condition Assessment Survey requires the periodic inspection of PP&E to determine their current condition and provide a cost estimate to make necessary repairs.

Major Classes of Real Property

For the purposes of this policy, the major classes of real property are:

- Buildings
- Structures
- Land
- NOAA-controlled capital leases-when NOAA has the financial responsibility for maintenance of the real property

Reporting

The following information shall be presented as required supplementary stewardship information:

- Identification of each major class of asset for which maintenance has been deferred.

- Method of measuring deferred maintenance for each major class of PP&E.

If the Condition Assessment Survey Method of measuring deferred maintenance is used, the following must be presented:

- \$ description of requirements or standards for acceptable operating condition
- \$ any changes in the condition requirements
- \$ asset condition and a range estimate of the dollar amount of maintenance needed to return it to its acceptable operating condition.

Method of Reporting

NOAA currently has a Capital Improvements Program database for real property assets, which includes an element that identifies deferred maintenance, the class of the asset, the estimated cost of each project, the prioritization of the items, records project funding, and notes completion of projects. That database will be used to report NOAA's deferred maintenance. Maintenance considered but not included in this database is determined to be immaterial.

Criteria for Inclusion

Deferred maintenance determination will only be made for:

- NOAA-owned properties meeting the \$200,000 capitalization criteria
- NOAA-controlled capital leases when NOAA has the financial responsibility for maintenance to the real property
- Individual deferred maintenance projects with a cost less than \$50,000 will not be considered.

Requirements or Standards for Acceptable or Operating Condition

Real property assets will be evaluated utilizing the following standards:

- Applicable building codes, and/or
- Manufacturer's operating specifications.

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Leases**

A lease is defined as an agreement conveying the right to use property, plant, or equipment (land, depreciable assets, or both), usually for a stated period of time. For financial statement reporting and disclosure purposes, leases are classified as either capital or operating based on specific criteria.

Capital Leases

Capital leases are contracts or agreements for the use of personal or real property items that possess the characteristics of a purchase. FASAB 5 defines a capital lease as a “lease that transfers all the benefits and risks of ownership to the lessee.” A lease is classified as capital if one or more of the following principal conditions are met at its inception:

1. The lease transfers ownership of the property to the lessee by the end of the lease term.
2. The lease contains an option to purchase the lease property at a bargain price.
3. The lease term (base period plus any option periods) is greater than or equal to 75 percent or more of the remaining estimated economic useful life of the leased property.
4. The present value of the lease payments, excluding executory costs, over the lease term (base period plus any option periods) equals or exceeds 90% of the fair market value of the leased property.

Criteria (3) and (4) do not apply if the beginning of the lease term falls within or beyond the last 25 percent of the total estimated economic life of the leased property.

Discount Rate

The discount rate to be used in determining the present value of the minimum lease payments ordinarily would be the lesser of 1) the lessee’s incremental borrowing rate, or 2) the lessor’s implicit rate computed in the lease. For federal government leases, the lessee’s incremental borrowing rate shall be the Treasury borrowing rate for securities of similar maturity to the term of the lease.

For all leases in effect prior to FY 1998, a copy of the Federal Reserve Statistical Release must be in the file to support the Treasury bond yield rate used in the spreadsheet calculation.

Beginning in FY 1998, it will be the real property branch’s policy to use the Nominal Discount Rate on Treasury Notes and Bonds of Specified Maturities rates, in accordance with the policy prescribed by the NOAA Finance Office. The Nominal Discount Rate on Treasury Notes and Bonds of Specified Maturities is contained in OMB Bulletin A-94 and the current rate is located in Appendix C. This document can be found on the Internet at:

<http://www.whitehouse.gov/omb/circulars/a094/a094.html>

Documentation supporting the rate used must be in the lease file. Attachment 7 contains the current rate and will be updated February 1 of each year to reflect the new rate. The rate used should match the length of the lease. If the rate is not given, then the rate should be determined by interpolation (average of rates given to approximate appropriate rate).

A Capital Lease Financial Data Spreadsheet (See Attachment 2) dating from the inception date of the lease must be used for initial determination of a capital or operating lease and must remain in the file for the remainder of the lease. If the initial capital lease spreadsheet is incorrect as a result of new information or the discovery of an error, the depreciable basis must be verified against the RSMIS depreciation module to ensure accuracy, and, if not in agreement, RSMIS should be updated.

New spreadsheets must be completed each fiscal year for each ensuing year of the lease for financial statement reporting. An example of this spreadsheet is provided as attachment 2.

Regardless of inception date, capital leases will be assigned object class codes of 3230 for building/storage leases and 3231 for land leases.

If the Fair Market Value of a leased property is less than the capitalization threshold of \$200,000 the lease is automatically an operating lease.

If it is not possible to determine the fair market value of a lease and the leased space is only for a part of the building the lease will automatically be classified as an operating lease. All possible methods of obtaining the fair market value must be exhausted. A memo must be placed into the file documenting this result.

Guidelines for Classifying Leases

The four principal capital lease criteria described above are standards in financial accounting. In addition to these criteria, NOAA has established a set of secondary criteria in determining whether a lease is capital or operating. They are:

1. Leases with a term less than or equal to one year should be classified as operating leases. Footnote disclosure is not required.
2. Leases with a term greater than one year but less than two years and total lease payments greater than or equal to \$200,000 should be classified as operating leases. Information regarding future minimum lease payments must be obtained for footnote disclosure requirements.
3. Leases with a term greater than or equal to two years and total lease payments greater than or equal to \$200,000 should be classified as operating leases if none the four principal capital lease criteria are met. Again, future minimum operating lease payments must be obtained for footnote disclosure requirements.
4. Leases with a term greater than or equal to two years and total lease payments greater than or equal to \$200,000 should be classified as capital leases if one or more of the four principal capital lease criteria are met. The capital lease should be recorded as a property asset at the

lesser of 1) the present value of rental and other minimum lease payments, or 2) fair value with an offsetting capital lease liability.

Leases Exempt from Capital Lease Consideration Include:

GSA Assignments

NOAA enters into lease agreements with the General Services Administration (GSA) for the use of building space and/or land. These are referred to as GSA assignments and are only applicable in real property. All GSA assignments should be classified as operating.

Tower Leases

NOAA enters into leases for space on towers. For example, NOAA could rent space on a tower and place an antenna on that space. These leases should be classified as operating. However, if leased tower space is used for a purpose other than the normal storage of transmitter equipment, it could be a capital lease.

Special Agreements to be treated as Operating Leases

License: An agreement between the federal government and a non-federal government entity by which the federal government occupies land or a facility for a specific purpose, often at no cost or at a cost for utilities and other operating expenses only.

Easement: A legal interest in land by which the federal government acquires the right to use land for a specific purpose and for a specific period of time, sometimes perpetual, such as for installation of utilities. This usually involves a one-time fee to obtain the right of way, which is recorded as a deed of easement.

Permit: An agreement between federal agencies by which one agency acquires the right to use land or facilities from another agency for a specific purpose, usually at no cost, although there may be reimbursement for utilities and other operating expenses.

Operating Leases

Any lease not meeting at least one of the capital lease criteria is classified as an operating lease. FASAB defines an operating lease as “an agreement conveying the right to use property for a limited time in exchange for periodic rental payments.”

Escalations/De-Escalations for Operating Leases

Because RSMIS cannot account for escalations or de-escalations in future lease payments, the **NOAA Operating Leases with Fixed Escalations/De-Escalations Spreadsheet** (See Attachment 6) must be used to determine the correct amount of future lease payments. This spreadsheet captures the actual lease payments and calculates the amount by which the finance office will need to adjust the RSMIS balance at the end of the fiscal year. RSMIS should show only the current annual rent payment. This does not apply to leases with escalations based on the consumer price index, nor does it apply to capital leases, which utilize a different spreadsheet to capture fixed escalations and other pertinent information.

The Lease Determination Worksheet

The NOAA Real Property Capital/Operating Lease Determination Worksheet (See Attachment 4) is used to determine the proper lease classification (capital or operating). It is divided into three parts:

Part I	Operating lease determination
Part II	Capital lease determination
Part III	Determination and signature

Part I is designed to determine if a lease is an operating lease. If the lease represents any one of the lease types listed in Part I of the worksheet, then the lease will be an operating lease and Part II does not need to be completed.

Part II is designed to determine if the lease meets any one of the four capital lease criteria. If the lease is not one of the lease types listed in Part I, then Part II is completed to determine if the lease should be capitalized. If criteria 1 or 2 are met, the lease will be capitalized and amortized over the remaining economic life of the property. If criteria 3 or 4 are met, the lease will be capitalized and amortized over the lease term or the remaining useful life, whichever is less.

Part III is used to document the lease determination based on the results of Part I and Part II.

The real property branch currently uses the NOAA Real Property Capital/Operating Lease Determination Worksheet dated June 9, 1999 (See Attachment 4) as the NOAA standard for all new leases. Leases entered into prior to the current worksheet date will not be subject to this worksheet.

All leases must have a lease determination worksheet placed in the file. This worksheet should be fully completed, signed, and dated; the effective date on the lease agreement (or SLA) should be used in determining if it is capital or operating. If necessary, an additional memo should be placed in the file with the worksheet to explain in more detail how the determination of capital or operating lease was made, how the FMV was calculated, how the land and building portions of the lease, if appropriate, have been separated, etc.

Additional Lease Policies

Leases Involving Land Only

If land is the sole item of property leased, and either of the first two capital lease criteria apply, it is recorded as a capital lease. Otherwise, it shall be treated as an operating lease. Because land is not depreciated, the economic useful life is difficult to determine; thus, only the first two criteria are considered for parcels of land.

Leases Involving Land and Buildings

If either of the first two capital lease criteria is met, the lessee shall separately capitalize the land and building. For this purpose, the present value of the minimum lease payments after deducting executory costs, including any profit thereon, shall be allocated between the two elements in

proportion to the fair market values at the inception of the lease. The amount allocated to the value of the building shall be amortized over the lease term. Parking lots should be considered in the building or structure cost.

Land Value is Less than 25% of Total FMV

If neither of the first two criteria for capital leases is met, and if the fair market value of the land is less than 25% of the total fair value of the leased property at the inception of the lease, the lessee shall consider the land and building as a single unit and apply the third and fourth criteria for capital leases. If either criteria 3 or 4 apply, the lease shall be considered capital, with both the land and the building being amortized over the term of the lease.

Land Value is more than 25% of Total FMV

If the value of the land is greater than 25% of the total fair value of the lease property, then the land and building need to be considered separately for the third and fourth capital lease criteria. If criteria 3 or 4 apply, the lease is capital and the building will be amortized over the term of the lease. Otherwise, it should be considered an operating lease. **The executory costs will be allocated entirely to the building.**

Buildings constructed on a leased parcel of land are to be tracked separately from the land, if the building is a capital lease and the land is an operating lease (or vice versa). The building should be given the same lease numbering as the land, with the designation “-A” added to the end of the number. (For additional information on tracking land and buildings separately, refer to chapter 3, page 3-9 of the NOAA lease-training manual.)

Fair Market Value

The Fair Market Value (FMV) of a real property lease or capital asset must reflect its value as of the lease inception or acquisition date. FMV determinations conducted prior to the acquisition date must be escalated forward to the acquisition date using consumer price index (CPI) rates; FMV determinations performed after the acquisition date must be discounted back to the acquisition date, also using CPI rates. However, FMV determinations dated six months prior to or later than the acquisition date will be deemed acceptable and will not warrant an adjustment. A copy of the CPI news release and the calculations must be in the file.

The following hierarchy of documentation sources will be used to determine fair market value:

1. A signed and dated appraisal performed by an independent party as of the inception date of the lease.
2. A letter from the lessor stating the fair market value of the leased property as of lease inception or sufficient information to determine fair market value (e.g., cost per square foot). A memo to the file stating how the FMV was determined must be placed in the file along with the letter from the lessor. (Records of phone calls to the lessor have been deemed inadequate because the auditor's have not been able to verify the information.)
3. Tax records may be used to determine FMV *if* the tax record is dated at least one year after the lease inception.

4. An income approach is acceptable to use to determine the FMV (See Attachment 3), which uses standard rates, actual expenditures, and square foot rental amounts to calculate the estimated property value. The sources used in the calculations must be properly documented.

Fiscal Funding or Cancellation Clauses in Leases

As discussed in FASB Technical Bulletin No. 79-10, Fiscal Funding Clauses in Lease Agreements, paragraph 3:

Paragraph 5(f) of Statement 13 requires that a cancelable lease, such as a lease containing a fiscal funding clause (a clause that generally provides that the lease is cancelable if the legislature or other funding authority does not appropriate the funds necessary agreement), be evaluated to determine whether the uncertainty of possible lease cancellation is a remote contingency. That paragraph states that “a lease which is cancelable (I) only upon occurrence of some remote contingency . . . shall be considered ‘non cancelable’ for purposes of this definition” of lease terms.

Cancellation clauses should not prohibit lease agreements from being capitalized.

Therefore, if a lease agreement meets all other capitalization criteria except for the non-cancelable criterion, the likelihood of the lease being canceled must be evaluated. If the possibility of cancellation is remote, the lease should be capitalized.

If a lease will be terminated prior to the final expiration date, the real property chiefs will verify that the lease expiration date in RSMIS has been changed to reflect the new expiration date. Files containing spreadsheets must be changed as well so that future lease payments will not be overstated.

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OMB 97-01 Capital Lease Reporting**

Capital Lease reporting which is addressed under SFFAS #5 discusses the proper amount to be recorded by the lessee as a liability under a capital lease. SFFAS #5 requires that “during the lease term, each minimum lease payment must be allocated between a reduction of the obligation and interest expense so as to produce a constant periodic rate of interest on the remaining balance of the liability.” For each capital lease, an amortization schedule must be completed identifying the rate of interest, the beginning balance, principal payments, interest expense, executory costs, and the ending balance.

Also, SFFAS #5 requires that “capital leases entered into during FY 1992 and thereafter are required to be fully funded in the first year of the lease.” The value to be funded is reported on the capital lease amortization schedule. Securing funding for capital leases is the responsibility of the NOAA Office of Management and Budget.

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Capital and Operating Lease Spreadsheet Preparation**

Capital and Operating Lease Spreadsheets need to be updated each fiscal year for reporting requirements.

Spreadsheets must be updated on the anniversary of the lease because that is when the lease amounts are typically adjusted. This will also allow more time for review and help us to efficiently manage the workload at fiscal year end.

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Estimated Executory Costs**

SFFAS No. 5 states “If the portion of the minimum lease payments representing executory cost is not determinable from the lease provisions, the amount should be estimated.” The estimate should be based on another lease with similar characteristics such as type of building, quantity of space, amount and type of services provided, location, and rental payments.

The following example illustrates the method to be used to estimate executory costs when the costs are not provided in the lease.

	Original Lease	Similar Lease
Yearly Rent(incl. exec costs)	\$240,000.00	\$360,000.00
Executory Costs	unknown	\$45,000.00
Length of Lease	20 Years	20 Years

Executory Costs on Similar Lease = $\$45,000 / \$360,000 = 12.5\%$

Executory Costs on Unknown Lease = $.125 \times \$240,000 = \$30,000$

Amounts to be reported on Capital Lease Financial Data Sheet

Gross Rent	Exec. Costs	Net Rent
\$240,000	\$30,000	\$210,000

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Holdovers/Supplemental Lease Agreements**

Leases in Holdover

In some instances after the expiration of the lease, the Federal government may opt to retain possession of the premises. This may be the result of on-going negotiations with the lessor. During this time, rent must be paid on a month-to-month basis at the rate during the previous lease term. Leases in holdover exceeding \$200,000 will be given a defined period for expiration in RSMIS, and, if no period is determined, the expiration date must be extended to the end of the current fiscal year.

Supplemental Lease Agreements (SLA's)

All Supplemental Lease Agreements must be completed on the Standard SLA form. Supplemental Lease Agreements (SLAs) represent revisions to the original lease agreement to include: 1) changes to the lease, such as deleting or acquiring additional square footage, 2) operating costs escalation based on the percentage change in the Consumer Price Index (CPI), 3) payment of a portion of the lessor's Real Estate taxes, if applicable; and 4) changes in the lessor's address. When a lease is extended through a supplemental lease agreement beyond the initial base term, RSMIS will be changed to reflect the effective date of the extension as well as the new expiration date.

An SLA signed by a Real Property Contracting Officer is documentation of agreement to changes in the lease terms, becomes part of the lease, and is filed with the lease. The RSMIS database manager then enters the changes into RSMIS, makes a printout of the changes, initials and dates the printout. To ensure accuracy, a Realty Specialist or Contracting Officer then initials the printout and places it in the file. This review must be performed by someone other than the preparer.

If a supplemental lease agreement modifies the quantity of space leased, the lease payment amount (other than operating costs), or the fair market value of the space, the lease must be considered as a new lease with an effective date of the supplemental lease agreement. The lease must then be evaluated to determine if it is an operating or capital lease.

Leases with Indefinite Expiration Dates

These leases contain a renewal option that is automatically exercised unless the government gives a written notification within 90 days. For reporting purposes, these leases are given an expiration year of 9999 in the RSMIS system to show the current year cost as well as project one fiscal year thereafter. Leases with indefinite expiration dates may be terminated at any time.

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Leases that approximately total \$200,000, but are Inaccurately Recorded in RSMIS

It is possible for leases that approximately total \$200,000.00 to be recorded incorrectly in RSMIS. The leases are recorded incorrectly due to an escalation or de-escalation clause in the lease agreement. The following example illustrates this problem.

Example:

5 Year Lease for Tower

Payment Schedule

Year 1:\$48,000.00

Year 2:\$44,000.00

Year 3:\$40,000.00

Year 4:\$32,000.00

Year 5:\$32,000.00

Total: \$196,000.00

Because year one is for \$48,000.00, RSMIS will report this lease in the Lease Disclosure Report, \$200,000 or Greater. This lease should not be reported on the Financial Statements because it is less than \$200,000. The spreadsheet must correct this by adjusting the Total Lease Liability downward by the total lease amount. Below are the adjustment amounts.

Year 1:(\$48,000.00)

Year 2:(\$44,000.00)

Year 3:(\$40,000.00)

Year 4:(\$32,000.00)

Year 5:(\$32,000.00)

Total: (\$196,000.00)

It is also possible for the opposite result to occur and have a lease reported as less than \$200,000.00 when the true total is more than this amount. The following example illustrates this problem.

Example:

5 Year Lease for Tower

Payment Schedule

Year 1:\$36,00.00

Year 2:\$36,000.00

Year 3:\$40,000.00

Year 4:\$44,000.00

Year 5:\$48,000.00

Total: \$204,000.00

Because year one is for \$36,000.00, RSMIS will report this lease in the Lease Disclosure Report, Leases from \$25,000 to \$199,999. This lease should be reported on the Financial Statements because it is more than \$200,000. The spreadsheet must correct this by adjusting the Total Lease Liability upward by the total lease amount. Below are the adjustment amounts:

Year 1:\$36,000.00
Year 2:\$36,000.00
Year 3:\$40,000.00
Year 4:\$44,000.00
Year 5:\$48,000.00
Total: \$204,00.00

To ensure that this problem does not occur, the real property chief should check the total payment over the lease term and confirm that the lease is reported properly in RSMIS.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Line Office Review**

The real property branch at NOAA headquarters will request the line offices to perform a 100% inventory review of real property to validate the accuracy of RSMIS and the integrity of the financial statements. The data contained in the property module will be used for the line office review. This request will be made annually during the second quarter of each fiscal year. It is the responsibility of the line offices to ensure that these reviews are completed in a timely manner. The CFO will be notified if any of the line offices do not respond by the due date.

At the end of the fiscal year, the real property chiefs will ensure that all pertinent lease information and all owned assets have been entered in RSMIS for proper financial statement reporting. The Real Property Chief will verify with realty specialists and engineers that real property is in compliance with the timely recording of real property items.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Capital Improvements**

This section establishes NOAA policy for determining whether a capital improvement to a building extends its useful life and how improvements to real property are to be depreciated.

Note: The cost threshold for placing capital or leasehold improvements in RSMIS is \$200,000 or greater. No improvement under this amount should be in RSMIS.

Improvement projects usually consist of repair or renovation to one or more of three major building systems: architectural, mechanical, or electrical. These major systems may be further divided into subdivisions as follows:

Architectural

- a) roofing and roof insulation;
- b) exterior finishes, doors and windows;
- c) interior finishes and partitions
- d) structural repairs and improvements

Mechanical

- a) plumbing and fire suppression;
- b) heating, ventilation, fuel storage and controls;
- c) chillers and cooling towers

Electrical

- a) service entrance and emergency power;
- b) distribution panels, uninterruptible power supplies, power conditioners, and alarm systems;
- c) interior and exterior lighting

Generally, for a project to be considered life extending, it should involve two or more major building systems and include the complete replacement or major renovation of at least three subdivisions. This is the general rule and is not intended to cover every situation. However, it will serve as a guideline for an engineering evaluation as to whether the project should be capitalized. **There may be projects—such as the complete replacement of a single major system—that would be life extending and thus capitalized. Projects of this type will be evaluated using the professional judgement of the engineer designing or overseeing the design of the project.**

Improvements must be supported by file documentation and must include a memo to the file (See Attachment 5) stating that the improvement was/was not life extending and should/should not be capitalized. The memo must be signed and dated by the engineer or other individual with specific knowledge of the project's cost and scope as outlined above.

Additionally, supporting documentation for the cost and useful life of the improvement must be kept in the lease file.

Furthermore, if multiple improvements are made under one alteration contract, there must be

documentation in each file to support the portion of the total contract dedicated to each specific capital improvement. RSMIS must reflect *actual costs*. The costs recorded must be the costs incurred during the year the improvement was constructed/installed.

Accounting for depreciation shall be performed as follows:

- a) If an improvement to a building does not extend the useful life of the building, the improvement should be expensed.
- b) If an improvement to a building does extend the useful life of the building depreciation should be calculated as follows:

Terminate Depreciation

1. Terminate the existing depreciation record as of the date the improvement is put into service. Retain a record of accumulated depreciation.

Life Determination

2. The new useful life equals the sum of remaining life of the building plus the additional amount of useful life gained by the improvement (as determined by the engineer).

Asset Value Determination

3. The new asset value equals the cost of the improvement plus the net book value of the original asset.

Depreciation

4. Depreciation is determined by dividing the new asset value by the new useful life.

Note: *The life extension procedure in the Depreciation Module within RSMIS should be used.*

An example of a life extending procedure: In August 1993 a building is purchased for \$1,477,020 and has an estimated useful life of 40 years (480 months). The monthly depreciation is \$3,077.12 (\$1,477,020/480). In March 1998 (after a period of 55 months), a life extending capital improvement is performed. The cost of the improvement is \$316,122 and increases useful life by 25 years (300 months). The calculation for determining the new depreciable basis and new useful life is presented here:

	Depreciable Basis	Useful Life in Months
Original cost	\$ 1,477,020.00	480
Depreciation prior to life extending procedure	\$ (169,241.00)	(55)
Net Book Value and useful life	\$ 1,307,779.00	425
Cost of improvement	\$ 316,122.00	300
New depreciable basis	\$ 1,623,901.00	725

Although RSMIS will perform the above calculations, in order to verify that the value and useful life of the improvement have been correctly entered into RSMIS, the following check should be performed. The total of the original asset plus the improvement must equal the total of the new asset record plus the depreciation prior to the life extending procedure. **This control should be performed for both the depreciable basis and the useful life.**

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Land Improvements**

Land is not a depreciable asset because it has an indefinite life. The Federal government has an immense amount of land that is used for diverse purposes. Land that is acquired or in connection with other general PP&E is defined as general PP&E and must be reported on the balance sheet.

When the government purchases land, its acquisition costs include any additional costs incurred to place the land in use. Improvements can be made at the time of acquisition or subsequent to acquisition. This includes easements, rights of way, appraisal costs, legal fees, surveying, draining, clearing, grading, tree clearance, filling (without paving or structures), leveling for facilities testing and parking areas, removal of structures or facilities purchased but not used, inspection costs, and landscaping.

Improvements that are included in the construction contracts for buildings or structures will be capitalized with the building or structure.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Capital Improvements to Land**

The position paper dated June 18, 1996 written by KPMG was to document our understanding of the proper accounting treatment of costs incurred subsequent to acquisition of real property.

Under the heading Improvements to Land, beginning with the second paragraph, the paper states, “The costs of improvements having a limited economic life such as landscaping, streets, sidewalks, and sewers should be debited to a Land Improvements account and depreciated over their economic lives. Whether these types of costs are incurred at the time of acquisition or subsequent to acquisition of the land, they should be capitalized separately and depreciated over their estimated economic useful life.” The third paragraph states, “If the local government authority is responsible for the continued upkeep of the improvements, then effectively the improvements have an indefinite economic life to the company and therefore should be added to the cost of the land. This is true regardless of when the improvements are obtained, at the time of acquisition or subsequent to acquisition.”

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
NOAA as Lessor**

The Office of Management and Budget (OMB) requires NOAA or BXA to disclose financial information on leases where NOAA or BXA is the lessor. A review should be performed annually on all NOAA and BXA outstanding reimbursable agreements; and all leases involving NOAA's or BXA's assets that have projected receipts should be identified. Moreover, NOAA is required to disclose agreements where income is received beyond compensation for maintenance and operation.

To assist Headquarters in gathering data relating to situations such as these, all ASC's should submit annually to the Chief, Real Property Management, copies of agreements that include payments of rent beyond reimbursement of utilities and maintenance. Once all information is received, Headquarters will prepare a summation for the finance office and forward a copy to the ASCs at fiscal year end.

Because the line offices may have entered into agreements that are unknown to the ASCs, every August the NOAA Finance Office will prepare letters to the Management and Budget Chiefs soliciting copies of these agreements from the line offices.

The Finance Office will be responsible for calculations and financial treatment of the Lessor agreements.

US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Acquired PP&E through Donation, Devise or Judicial Process

The position paper dated June 18, 1996 written by KPMG was to document our understanding of the proper accounting treatment of costs incurred subsequent to acquisition of real property. The first sentence under the heading of Improvements to Land states “The original acquisition cost of the land is the actual amount paid for the land and any additional costs incurred to place the land in use.” If the land is acquired through donation, devise, or judicial process excluding forfeiture the land is valued at fair market value.

The position paper references SFFAS NO. 6. Paragraph 30 of SFFAS NO. 6 that states, “The cost of general PP&E acquired through donation, devise, or judicial process excluding forfeiture shall be estimated fair market value at the time acquired by the government.” The position paper also references NAO 203-157 which states under the heading of PURCHASED and LEASED-TO-PURCHASE LAND REPORT, subheading Acquisition Cost, “if donated, acquired by seizure, or foreclosure, insert the fair market value plus any costs incurred to place the land in use.”

If a property donor elects to waive an appraisal, the title insurance valuation may be used to determine the fair market value of the donated property. Notification from the donor stating that an appraisal has been waived must be kept on file.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Excess Real Property**

The Real Property staff is responsible for reporting excess property in accordance with Federal Property Management Regulations, Chapter 101-47.202.

In the event that notification of excess property is required, the acquisition cost on the excess report must be taken from RSMIS.

Notification from the vacating office stating when the property has/will cease from use must be documented in the file. It is the responsibility of the Realty Specialist/Database Manager to remove real property and accumulated depreciation from RSMIS when the property is no longer beneficial to NOAA's operations. Specifically, when NOAA no longer utilizes the property, the property should be removed from the depreciation module. ***Note: The property cannot be removed from the property module until it has been disposed of.*** Therefore, the property remains the holding agency's responsibility and consequently in the agency's inventory until disposal is completed.

For excess property that must be reported to GSA, Form 118; "Report of Excess Property" is required. The cost information on this form should agree to the supporting real property documentation file as well as the recorded amount in RSMIS.

To ensure the accuracy of the data, the Real Property Supervisor prior to submittal must review all excess reports.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Stewardship Property, Plant, & Equipment (PP&E)**

Stewardship PP&E

“Form and Content of Agency Financial Statements,” OMB 97-01, requirements include reporting of Stewardship PP&E. Federal Mission Assets, Heritage Assets, and Stewardship Land are the three classes of Stewardship PP&E. These assets will be recorded different from the general PP&E and should be reported separately on the Statement of Net Cost or disclosed in the footnotes. It has been determined that NOAA’s Real Property Community is responsible for reporting Heritage Assets only.

Heritage Assets

Heritage assets are unique and are generally expected to be preserved indefinitely. They are held for their historical, cultural, educational, and architectural style. These assets are reported in units versus cost. Examples of heritage assets include the Lincoln Memorial and the Washington Monument.

Multi-use Heritage Assets

Multi-use Heritage assets serve dual purposes. Not only do they remind society of our heritage; they are also used in daily governmental operations. Examples of multi-use heritage assets include the White House and the US Treasury building.

Method of Data Collection for Supplementary Financial Statement Reporting

The ASCs are responsible for reviewing their real property portfolios and reporting these types of assets to headquarters as part each annual fiscal year end data call. If doubt exists regarding the eligibility of an asset to be considered a heritage or multi-use heritage asset, the prevailing rule of thumb will be to report it. An example of acceptable reporting is included in these policies as attachment 8. Headquarters will review these submissions with NOAA Finance for final determination on whether or not to classify these items as Heritage or Multi-Use Heritage assets. The ASC’s will be notified of exclusions to eliminate the need to submit future updates on the excluded properties.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Transfer of Real Property to NOAA from another Federal Entity**

Recording the Transfer of Real Property from another Federal Entity

Effective June 1, 1998, in the RSMIS property module, assets acquired by NOAA from other Federal agencies should be recorded at the net book value reflected in the transferor's books. If cost information is not available, the cost of the asset should be recorded based on the property's Fair Market Value at the time of transfer. It should be noted that this is a change from previous real property policy, which stated, "are shown in the RSMIS property module at the prior entity's original acquisition cost and date."

The RSMIS depreciation module will reflect the net book value upon transfer, and NOAA's acquisition date. If the asset equals or exceeds \$200,000, depreciation will be taken over the remaining useful life of the asset that was assigned by the transferor. If the asset is less than \$200,000, the item will not be capitalized, but must be reflected in the master file.

Upon acquisition of the asset, NOAA has the option to assign a different useful life based on the period it expects to obtain benefit from the asset; however, one must justify this useful life in writing and incorporate it into the Real Property file. One must be mindful that this period must not exceed the standard useful lives prescribed by NOAA.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Accounting Treatment for Prepaid Rent**

Prepaid Rent

There are some instances in which cash flow precedes recognition of the related expense. An example is prepaid rent. Prepaid rent is a rent payment that is made in advance of the related expense recognition.

NOAA has prepaid rent for a few operating leases. The ASCs have an obligation to track prepayments annually and forward the information to Headquarters, which will submit the information to the Finance office. Finance will prepare the necessary entries to properly classify this cost.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
Prior Period Adjustments**

Disposal of Leases or Assets

If an asset has been entered into or deleted from RSMIS during the current fiscal year, but the acquisition or disposal actually occurred during a prior year, the asset will be recorded as a prior year adjustment. That is, the amounts should be recorded as adjustments to the previous fiscal year's balances. Likewise, any such future occurrences should be recorded in the prior year's balances, *not* the current year's. Any owned properties that have been acquired or disposed of during any given fiscal year must be tracked.

This policy is only applicable to assets equal to or greater than the \$200,000 threshold.

**US Department of Commerce
National Oceanic and Atmospheric Administration (NOAA)
Internal Control Policy
CWIP Confirmation**

Appendix C in the Construction Work-in-Progress Policy and Procedure manual details the Construction Work-in-Progress Processing Flow and Responsibilities (General). Part III; numbers 18-20, establish the procedure for reporting the project to real property and its subsequent recording in RSMIS.

18. The CWIP Task Manager will send the completed original of the Form 37-6, together with the file containing all documentation to support the costs summarized on the form, to the appropriate Property Office.
19. The Property Office will review the Form 37-6 and file documentation for completeness. Incomplete files will be returned, along with the Form 37-6, to the CWIP Task Manager for correction. If all information is complete in the file, the Property Office will record the capital asset in RSMIS (Real Estate and Space Management Information System).
20. The relevant Property Office will annotate the Form 37-6 to indicate data entry to the appropriate system and send a copy of the annotated Form 37-6 to OFA Finance.

It is important to note the following supplemental instructions for processing Form 37-6:

- The CWIP Task Manager must complete the “FROM” box at the top right of the form including his/her signature in the designated block.
- Upon completion of the project, the task code should be one that correctly represents NOAA’s strategic objective. Typically, this information is reported by the Line Office budget contact.
- Any changes made after submitting the original Form 37-6 requires a revised form to be completed. The modified Form 37-6 must be prepared and submitted in the same method as the original and must be clearly marked as a revision.
- If possible, validate that the useful life of the asset is in compliance with NOAA’s policy.

In addition, the Disposal of Leases or Assets policy implements two procedures to ensure that CWIP projects are recorded in a timely manner. The first is a request to the line offices to perform a 100 percent inventory review of real property to validate the accuracy of RSMIS. The second is that the real property chiefs will verify policy compliance with the project engineers.

